



ADAPTATION FUND

AFB/B.29/6
3 March 2017

Adaptation Fund Board
Twenty-ninth meeting
Bonn, Germany, 16-17 March 2017

Agenda item 10 b)

**STRATEGIC DISCUSSION ON OBJECTIVES AND
FURTHER STEPS OF THE FUND: POTENTIAL
LINKAGES BETWEEN THE FUND AND THE GREEN
CLIMATE FUND**

Background

1. At its twenty-fourth meeting the Adaptation Fund Board (the Board) requested the secretariat to prepare a document containing elements on potential linkages of the Adaptation Fund (the Fund) with the Green Climate Fund (GCF), for consideration during the intersessional period between its twenty-fourth and twenty-fifth meetings. The secretariat produced document AFB/B.24-25/1, *Potential linkages between the Adaptation Fund and the Green Climate Fund*, which was built upon the options outlined in document AFB/B.20/5, *Strategic prospects for the Adaptation Fund*, discussed at the twentieth Board meeting in March 2013. Document AFB/B.24-25/1 analyzed in particular two scenarios: (a) establishment of an operational linkage with the GCF, through either accreditation or an ad hoc agreement or memorandum of understanding; and (b) institutional integration between the two funds. By decision B.24-25/9 the Board decided to request the secretariat to further assess: (i) the potential for the Fund to apply as a financial intermediary of the GCF; and (ii) the feasibility of entering into some form of memorandum of understanding (MOU) or legal agreement under which the Fund could programme GCF funds; and present its conclusions to the twenty fifth meeting of the Board.
2. In accordance with the Decision B.25/26, the secretariat, in consultation with the trustee, prepared and presented Document AFB/B.26/5 to the Board for consideration at its twenty-sixth meeting which contained further legal, operational, and financial analysis on the implications of various linkages with the GCF. Document B.26/5 focused on option (i), outlined in decision B.24-25/9, of accreditation of the Fund as intermediary of the GCF, considering that option (ii) of entering into the Memorandum of Understanding or legal agreement to programme GCF funds may take similar approach to the option (i). In the ensuing discussion at the twenty-sixth meeting, in general, the Board was of the view that it was premature to seek accreditation under the GCF while there were differing opinions: some Board members saw accreditation as a means of ensuring the Fund's sustainability while others disagreed, and furthermore, stressed the need to separate the issues of linkages with the GCF and financial sustainability. It was noted that any operational linkage between the Fund and the GCF would need to avoid duplication and inconsistency of policies and procedures, reporting requirements, tracking of funds, and funding decisions in order to be effective and efficient.
3. Since the twenty-fifth meeting, the secretariat has continued interacting with the GCF secretariat in the areas identified by the Board to foster complementarity, namely accreditation, readiness support, results-based management and project pipeline.
4. The Conference of the Parties had, by decision 7/CP.21,¹ encouraged the GCF Board to improve its complementarity and coherence with other institutions, per paragraphs 33 and 34 of the governing instrument for the GCF² including by engaging with relevant bodies of the Convention, such as the Standing Committee on Finance.

¹ <http://unfccc.int/resource/docs/2015/cop21/eng/>.

² See at https://www.greenclimate.fund/documents/20182/226888/GCF_B.13_08_-_Complementarity_and_coherence_with_other_funds.pdf.

5. During the twenty-eighth meeting of the Board, in responses to queries about the partnership between the GCF and the Adaptation Fund, at the request of the Vice-Chair, the representative of the GCF explained different ways to establish linkages between the two Funds. He gave three examples. First, the GCF Board had recently decided that developing countries could apply for up to US\$ 3 million to support their national adaptation planning processes through the readiness programme of the GCF. That support would be delivered either through accredited partners or delivery partners that complied with fiduciary management capacity requirements. Second, accreditation was one form of partnership, a formal link with a partner that would either supervise or implement projects of behalf of the GCF. The GCF looked at two issues in accreditation: whether the partner met the required technical and fiduciary standards, environmental and social safeguards and the gender policy of the GCF, and why the partner was seeking a relationship with the GCF. He explained that the fit-for-purpose classification was a key concept of the accreditation system. The requirements had been categorized into a number of types that allowed different categories of entities to be accredited in ways that tailored the requirement to the types of activities that the entity wanted to undertake. Third example was enhanced direct access which provided resources to entities accredited to the GCF in order for them to fund small activities that were community-led or were at the local level; most of the direct access entities were interested in that programme. Most of those activities would be for adaptation; adaptation is important for the GCF, especially small scale activities, and consequently it would be necessary to establish relations with institutions with requisite experience.

6. Having considered document AFB/B.28/6 and the update provided by the secretariat, the Adaptation Fund Board (the Board) decided to:

a) *Based on decision B.27/37 and GCF Board decision B.13/12, request its representatives to be nominated by the Chair and the Vice-Chair, assisted by the secretariat, to attend an annual dialogue to be initiated by the Green Climate Fund (GCF) at the fifteenth meeting of the GCF Board in order to enhance complementarity;*

b) *Request the secretariat to:*

(i) *Continue discussing, with the GCF secretariat, concrete activities in the areas of complementarity and coherence identified by the Board in decision B.25/26; and*

(ii) *In consultation with the trustee, as appropriate, update document AFB/B.26/5, containing further legal, operational and financial analysis on the implications of various linkages with the GCF, for consideration by the Board at its twenty-ninth meeting;*

c) *Request the Chair and Vice-Chair to continue consultations with the co-chairs of the GCF on potential linkages between the Adaptation Fund and the GCF; and*

d) *Request the Chair and the secretariat to report to the Board at its twenty-ninth meeting on the progress made related to sub-paragraphs a), b) and c).*

(Decision B.28/4)

7. The current document responds to paragraph b) (ii) of Decision B.28/4 above, and presents further legal, operational and financial analysis on the implications of various linkages with the GCF.

Legal analysis

Fund legal capacity as a stand-alone organization

8. The basic fiduciary standards for accreditation with the GCF require, among other standards, that the entity must have the legal personality and the legal capacity to directly receive funds. In the case of the Fund established through Decision 10/CP.7, only the Board, as its operating entity, has legal personality.³ The Board supervises and manages the Fund, under the authority and guidance of the Conference of the Parties serving as the meeting of the Parties to the Kyoto Protocol (CMP), and is fully accountable to the CMP,⁴ and the Fund functions under the guidance of, and be accountable to the CMP.⁵ In addition, the Fund relies on the World Bank for trustee services in accordance with the Agreement on the Terms and Conditions of trustee services (“the Terms and Conditions”) concluded by the Board of the World Bank and CMP,⁶ and relies on the Global Environmental Facility (GEF) for secretariat services to the Board based on the Memorandum of Understanding between the Council of the GEF and CMP.⁷

9. In summary, the Fund has complexities inherent in its institutional governance and structure composed by:

a) The Fund Board is the operating entity of the Fund with legal personality based in Germany⁸ and supervise and manage the Fund under the authority and guidance of the CMP⁹;

b) The Global Environment Facility provides secretariat services to the Adaptation Fund Board on an interim basis¹⁰ through a dedicated team of World Bank Staff in a functionally independent and effective manner.¹¹ The GEF Instrument is neither signed nor ratified as a treaty. Instead, it has been incorporated in separate resolutions by the World Bank’s Board and the governing councils of UNDP and UNEP (and endorsed by the UN General Assembly). The World Bank does not consider the GEF a subsidiary organ of the World Bank nor the United Nations (UN).

³ Decisions 1/CMP.3 and 1/CMP.4. The Chair and Vice-Chair of the AFB jointly serve as legal representatives of the Board (Decision 1/CMP.5).

⁴ Decision 1/CMP.3.

⁵ Decision 28/CMP.1

⁶ Decisions 1/CMP.4; 5/CMP.6; 4/CMP.8; 1/CMP.9; 1/CMP.10; 2/CMP.12.

⁷ Decisions 1/CMP.4; 4/CMP.8; 2/CMP.10; 2/CMP.12.

⁸ Act to establish the legal capacity of the AFB in Germany (Gesetz zur Verleihung der Rechtsfähigkeit an den Rat des Anpassungsfonds in Deutschland (1 February 2011); Decision 1/CMP.4, paragraph 11.

⁹ Decision 1/CMP.3.

¹⁰ Decisions 1/CMP.4; 4/CMP.8; 2/CMP.10; 2/CMP.12.

¹¹ Decision 1/CMP.3 and the Memorandum of Understanding between the CMP and the Council of the GEF Regarding Secretariat Services to the Adaptation Fund Board.

c) *The World Bank* serves as the interim trustee of the Adaptation Fund by invitation of CMP under the Terms and Conditions in accordance with the applicable provisions of the World Bank's Articles of Agreement, by laws, policies and procedures.¹² On behalf of the Fund, the World Bank performs two core functions: it sells the Share of Proceeds (Certified Emission Reductions (CERs), Assigned Amount Units (AAUs) or emission reduction units (ERUs) collected as the share of proceeds for the Adaptation Fund)¹³ that help support the Fund and manages the Adaptation Fund Trust Fund.¹⁴

10. Under the accreditation standards of the GCF in order to achieve accreditation, an accreditation applicant entity needs to demonstrate a number of capacities, policies and systems including its general management and administrative capacity for accreditation: for instance, oversight authorities, audit committee, regulators, governing board, executive body, internal audit body, external audit body, etc. The Board, the World Bank (for the secretariat) and IEs share different aspects of these capacities, policies and systems needed for accreditation. At the Fund level, the trustee and secretariat services are covered by the single audit of the World Bank. At the level of operations, the Fund relies on the fiduciary rules and procedures of the implementing entities and has (only) two regular ways of exercising oversight: the accreditation process and the project/programme review process, both of which take place under the supervision by the Board and include the Board as the approving body.

Operational Analysis

Compatibility of the legal obligations under GCF Accreditation Master Agreement (AMA) with the Board's functions and mandates guided by the CMP

11. The GCF uses a framework agreement, called the Accreditation Master Agreement (AMA), which has to be signed before the GCF and the accredited entity proposing a project enter into a project-specific agreement. Assuming that the Fund, as represented by the Board with legal personality, is accredited by the GCF, the Board represented by its Chair and Vice-Chair¹⁵ would be required to sign the AMA with the GCF. The nature and scope of the legal obligations that the accredited entity would be undertaking by signing the AMA with the GCF are outlined in an AMA template that was approved by the GCF Board in February 2016.¹⁶

¹² Decisions 1/CMP.4; 5/CMP.6; 4/CMP.8; 1/CMP.9; 1/CMP.10; 2/CMP.12; Terms and Conditions of services to be provided by the International Bank for Reconstruction and Development as trustee for the Adaptation Fund (hereinafter "Terms and Conditions of trustee services").

¹³ See *Terms and Conditions of trustee services, paragraphs 3, 9, 24-28.*

¹⁴ *Id.*, paragraphs 7, 17-23.

¹⁵ Under Article 1 (2) of the Act to establish the legal capacity of the AFB in Germany (Gesetz zur Verleihung der Rechtsfähigkeit an den Rat des Anpassungsfonds in Deutschland (1 February 2011) and Decision 1/CMP.5, the Chair and Vice-Chair of the AFB jointly serve as legal representatives of the Board.

¹⁶ See

https://www.greenclimate.fund/documents/20182/319135/Accreditation_Master_Agreement_Template.pdf/8c4f6cbf-ae17-4856-81c1-64ac8fbfa506.

12. Unlike the standard legal agreement between the Adaptation Fund Board and Implementing Entity, the GCF Board noted that the template AMA was a basis of negotiation with accredited entities, and allowed changes to its AMA with its accredited entity for fit for purpose on a case-by-case basis.¹⁷ However, If the changes are deemed as ‘substantive changes from the template AMA’, which materially affect the terms of the template AMA, the entity needs to meet certain conditions, follow the required process, and obtain the GCF Board approval.

13. One issue is whether the legal obligations outlined in the AMA are in line with the functions and mandates of the Board provided by the CMP. For instance, unless a special amendment for an AMA with the Adaptation Fund Board could be accommodated by the GCF Board, if the Board signs the AMA, it would be obligated to bear full accountability for implementation of the project/programmes to be funded by the GCF¹⁸, which a licensed lawyer in Germany would need to confirm if this would conflict with the Board’s privileges and immunities enshrined in the Act to establish the legal capacity of the Adaptation Fund Board in Germany. With respect to the Board’s privileges and immunities, it appears to be necessary to consult with a license lawyer in German law so that the Board would be aware of any amendments required or compliance issues.

14. In this regard, the template AMA as it stands would appear difficult for the Board to sign without addressing the issue of conflict between the legal obligations under the AMA and the Board’s privileges and immunities under German law as well as mandates and functions guided by the CMP. It is uncertain and beyond the scope of this document to determine whether these issues can be resolved through the ‘substantive changes’ to the template AMA.

15. Another issue is whether the Board is required to obtain approval by the CMP in the event that the Board decides to apply for accreditation with the GCF. This issue has been considered by the UNFCCC Standing Committee on Finance (SCF) in 2015, when it indicated in document SCF/2015/10/12 that: “there was broad understanding among SCF members that ‘institutional linkages’ could require a decision by the COP/CMP in most cases, while ‘relations’ would not”¹⁹; and in case the Board decides to pursue any of the options analyzed in Decision B.24-25/9 (applying as financial intermediary of the GCF and entering into MoU or legal agreement under which the Fund programmes GCF funds), it needs to be clarified on whether CMP decision needs to be obtained.

16. It is noteworthy that at the 9th meeting of the SCF, the committee noted that, “from a legal point of view, the Adaptation Fund is established under the Kyoto Protocol, which implies that the establishment of any institutional arrangements between the Fund and other institutions under the Convention which have legal implications would require decisions both by the COP and the CMP.”

¹⁷ See GCF Board Decisions B.12/31 and B.13/29.

¹⁸ The Board approves projects/programmes and is bound by the terms and conditions of the legal standard agreement with the implementing entities. The Board does not supervise implementing entities whereas implementing entities bear full accountability for implementation of the project/programme.

¹⁹ See document SCF/2015/10/12, Working paper on possible future institutional linkages and relations between the Adaptation Fund and other institutions under the Convention (Draft – version 9 June 2015, paragraphs available at http://unfccc.int/files/cooperation_and_support/financial_mechanism/standing_committee/application/pdf/working_paper_af_institutional_linkages_rev.pdf.

It is also worth considering that the Fund is in the process of becoming formally assigned to serve the Paris Agreement which has entered into force.²⁰ Depending on the timing of the Fund applying for accreditation and signing the AMA after being accredited with the GCF, the Board may need to obtain approval from the CMA along with the CMP and COP if it is mandated to serve the Paris Agreement by relevant CMA and COP decisions. These issues would require further clarification or guidance from the relevant authority such as the CMP or the Standing Committee on Finance.

Financial Analysis

Funds contributed by each donor cannot be earmarked for specific purposes

17. Under the Terms and Conditions, the Adaptation Fund Trust Fund held at the World Bank²¹ can receive two types of funding. First, the World Bank as the interim trustee can receive and hold in the Trust Fund any proceeds from the Sale of the Share of Proceeds²² conducted pursuant to paragraphs 24-28 of the Terms and Conditions.²³ Second, if requested by the Board, the Trustee may accept, on terms mutually agreed between the Trustee and the Board, contributions from donors to support the operations of the Adaptation Fund.²⁴ The amendments to the Terms and Conditions are effective only after adoption of the same by both the CMP and the World Bank .

18. As indicated in the Document AFB/B.26/5, the terms and conditions applicable to donations to the AF trust fund have been agreed by the Board and are the same for all donors contributing to the AF trust fund. Funds contributed by each donor cannot be earmarked for specific purposes²⁵ as all funds provided to the AF trust fund are pooled and allocated for use by the Board. If the Fund receives funding from the GCF as ‘contributions,’ and the GCF requires different terms and conditions for the use of its contributed funds, or requires its funds to be ‘earmarked,’ the AF Board would need to first agree to such exception to its policies and procedures. From a financial management perspective, it may also be necessary to request the Trustee to establish a separate

²⁰ See paragraphs 14-15 of Decision 1/CP.22 and paragraph 11 of Decision 1/CMA.1.

²¹ The Adaptation Fund is categorized as a Financial Intermediary Fund. As specified in the “The World Bank's distinctive role across FIFs is the provision of financial intermediary services, as Trustee of the funds. For all FIFs, the World Bank provides a set of agreed financial services that involve receiving, holding and investing contributed funds, and transferring them when instructed by the FIF governing body. Under some FIFs, the World Bank also provides customized treasury management or other agreed financial services; some examples include bond issuance, hedging intermediation and monetization of carbon credits”. (<http://fiftrustee.worldbank.org/Pages/FIFsOverview.aspx>).

²² The sale or disposal, for the purpose of monetization (Sale), or of certified emission reductions (CERs), assigned amount units (AAUs) or emission reductions units (ERUs) are collected as the share of proceeds for the Adaptation Fund. *Id.*, paragraph 3.

²³ See *Id.*, paragraph 17.

²⁴ *Id.*

²⁵ Under an MDTF, it is not possible to earmark funds by participating donors to specific activities or to specific recipients, i.e. the donors cannot earmark for a subsets of the purpose of the trust funds or subset of the countries if the trust fund is global in nature. However, donors may state a non-binding preference that their contribution be used to finance one or more specific sectors/themes, but without a legally binding commitment by the Bank.

(http://siteresources.worldbank.org/EXTEXTINDTRAINI/Resources/Donor_Guide_11-03-09.pdf)

trust fund at the World Bank to facilitate such earmarking (which may require approval at the level of the World Bank's Executive Directors).²⁶

19. The other issues to be clarified include: (i) whether a separate legal agreement between the GCF and the World Bank as AF trustee would be required to accept GCF funds into the AF trust fund; and (ii) the outcome of the GCF currently in the process of appointing the permanent Trustee.²⁷ The analysis of what could happen in the event the World Bank no longer serves as the interim trustee for the GCF after April 2018, is outside the scope of this document. However, a separate legal agreement between the new GCF trustee and the World Bank as AF trustee would be required to accept any cash transfer from the GCF into the AF trust fund at the World Bank.

20. It is noteworthy that as all funds are pooled in the AF trust fund, it will not be possible to track and return any investment income/loss in respect of GCF funds transferred to the AF trust fund, which is understood to be one of the GCF requirements in the AMA. The legal arrangements between the Board and the GCF would also need to be consistent (or at least not incompatible) with the financial management, reporting and other procedures of the trustee, in accordance with the respective legal arrangements between the World Bank and the CMP (for the Fund) and between the World Bank and the GCF (for the GCF).

21. The GCF funding could be considered as a non-sovereign entity donation, however the AFB can only follow the same rules of other un-earmarked funds to be allocated by the AFB, which may not be satisfactory to the GCF, that may require a more active involvement in approval, allocation, etc.

Overview on a legal agreement or Memorandum of Understanding (MOU) between AF and GCF

22. The other option presented in the AFB/B.26/5 was a legal agreement or MOU between the two funds. The document indicated that this option might allow more flexibility, if politically feasible, to tailor the MoU/legal agreement to the specific situations, features and types of projects/programmes funded by the Adaptation Fund and to come up with an option that may avoid duplication and inconsistency, and reduce administrative costs. The World Bank currently provides trustee service to both funds (on an interim basis).

23. Currently, the GCF has not signed the MoU for similar purpose that the Fund would seek, and political will from both parties would be imperative to embark on a negotiating process. It is also worth considering that along with other issues above, the issues relating to the Fund's accreditation with the GCF need to be further clarified or resolved to facilitate the negotiation for a possible MoU with the GCF, if the Board decides to do so.

²⁶ It is worth noting that if the CMP or the Board is to make a new decision related to the functions of the Trustee performed or to be performed under the Terms and Conditions, such a decision would have to be developed in close consultation with the Trustee in order for the Trustee to be bound by the decision of the CMP or the Board (*Id.*, paragraph 12)

²⁷ See Document GCF/B.15/15/Rev.01.